BEFORE

THE PUBLIC SERVICE COMMISSION OF

SOUTH CAROLINA

DOCKET NO. 2019-281-S

IN RE:	)	
	)	
Application of Palmetto Utilities, Inc.	)	**PREFILED REBUTTAL TESTIMONY**
for adjustment of rates and charges	)	**OF DONALD J. CLAYTON**
for, and modification to certain terms	)	**ON BEHALF OF PALMETTO**
and conditions related to,	)	**UTILITIES, INC.**
the provision of sewer service.	)	

Q. ARE YOU THE SAME DONALD J. CLAYTON WHO HAS PROVIDED DIRECT TESTIMONY IN THIS PROCEEDING?

A. Yes.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY IN THIS PROCEEDING?

A. The purpose of my rebuttal testimony is to take issue with positions taken by ORS and the consumer advocate with respect to the proposed hypothetical capital structure and cost of capital and the treatment of the former City of Columbia facilities in the revenue requirement.

Q. WHAT IS THE ORS'S POSITION WITH RESPECT TO COST OF CAPITAL FOR PUI?

A. ORS witness Parcell is recommending an overall cost of capital of 7.90%. His recommendation is based on a hypothetical capital structure of 45% debt and 55% Equity, a debt rate of 5.89% and an ROE of 9.55%.

Q. DO YOU AGREE WITH MR. PARCELL'S RECOMMENDATION?

A. No for the following reasons. First, there is no need to impose a hypothetical capital structure since Mr Parcell's own proxy group shows that PUI's actual capital structure is well within the range of capital structures for other water/wastewater companies. Second, Mr. Parcell chooses the midpoint of the range of ROEs for the proxy group and makes no adjustment to reflect the fact that PUI is much smaller than any company in the proxy group. Third, Mr. Parcell uses the Company's debt rate of 5.89% but makes no adjustment to reflect the fact that the company would be likely to have a higher debt rate if its actual capital structure included more debt (i.e. more debt leverage makes the company more risky).

Q. **WHAT COST OF CAPITAL IS MR. ROTHSCHILD RECOMMENDING?**

A. Mr Rothschild is recommending a cost of capital of 7.33% based on a 47.5% debt and 52.5% equity capital structure, 5.89% cost of debt and an 8.63% ROE. Mr. Rothschild relies heavily on his analysis of the impact of COVID-19 on the financial markets to arrive at his recommended ROE.

Q. **DO YOU AGREE WITH MR. ROTHSCHILD'S ANALYSIS AND COST OF CAPITAL RECOMMENDATION?**

A. No, for the reasons cited above with respect to Mr. Parcell's testimony and for the additional reason that the impact of COVID-19 virus should not reduce the company's cost of capital. If the impact of COVID-19 is to be considered at all it should increase the Company's cost of capital because the Company is now more risky with respect to revenue collection and increased cost of operations due to social distancing and other factors resulting from protecting employees and customers. Also, is not appropriate to include the financial impacts of this highly unusual period of historic market volatility to try to set a cost of capital underlying the rates that will be in effect for the next couple of years.

Q. **WHAT COST OF CAPITAL SHOULD THE COMMISSION ADOPT?**

A. The Commission should reject the positions of Mr. Parcell and Mr. Rothschild in favor of the Company's proposed overall return of 8.57% based on PUI's actual capital structure of 41.79 % debt and 58.21% equity and actual cost of debt of 5.89% and a 10.5 % return on equity as recommended by Company witness Harold Walker.

Q. WHAT ORIGINAL COST FOR THE FACILITIES ACQUIRED FROM THE CITY OF COLUMBIA IS INCLUDED IN THE RATE BASE IN THIS FILING?

A. The total original cost related to these facilities that is included in the rate base is $29.9 million related to the original acquisition in 2013 from the City of Columbia as shown in the February 28, 2013 study I prepared and which PUI provided to the Commission in the September 2019 allowable ex parte briefing, a copy of which is attached to my direct testimony as DJC Exhibit 3. When you subtract the accumulated depreciation, you get approximately $18 million of starting net plant value.

Q. WHAT IS THE ORS POSITION WITH RESPECT TO THE FACILITIES ACQUIRED FROM THE CITY OF COLUMBIA DETERMINED?

A. ORS witness Loy is proposing to reduce the Company's rate base related to these facilities from approximately $12 million to just $1.5 million. He makes a number of adjustments including post-closing tap fees recorded by the Company as revenue, the use of the Handy-Whitman index instead of the CPI-U to determine the original cost of the property acquired from the City of Columbia, and the presumption that there were significant developer contributions received by the City which should be reflected as CIAC by PUI.

Q. DO YOU AGREE WITH THE ADJUSTMENT S PROPOSED BY MR. LOY?

A. No. I do not agree with the adjustments proposed by Mr. Loy. I disagree with the adjustment to record post-closing plant expansion fees recorded as revenue. I disagree with the use of the Handy-Whitman index for the reasons described in my direct testimony. I also disagree with Mr. Loy's estimate of developer contributions to the City.

Q. WHY DO YOU DISAGREE WITH MR. LOY'S ADJUSTMENT TO RE-RECORD POST LOSING PLANT EXPANSION FEES FROM REVENUE TO CIAC?

A. I disagree with Mr. Loy's adjustment to recast post-closing plant expansion fees from revenue to CIAC because the ratemaking related to Palmetto of Richland County LLC ("PRC") was held in abeyance by the Commission until such time as the

Company sought a change in PRC base rates. The Commission allowed the Company to continue to charge the rates that were charged by the City including the plant expansion fees. As such the Company did not have a cost based rate structure and was not allowed to book the taps fees as CIAC under GAAP. To now go back and try to recast these items now as CIAC is not fair as the Company was under an entirely different rate regime which factored into their acquisition decision. To go back and recast tap fees now is akin to retroactive ratemaking and the Commission should not impose this adjustment on the Company. Further, since 2017 (when the Commission approved the merger of PRC into PUI for ratemaking purposes) the Company has not earned a return of or on the assets acquired from the City even though it has continued to depreciate these assets and use them to provide service to customers. In fact, no return has ever been earned on these assets since they were acquired in 2013.

Q. DO YOU AGREE WITH MR. LOY'S ADJUSTMENT TO IMPUTE DEVELOPER CONTRIBUTIONS RELATED TO THE ACQUISITION OF THE ASSETS FROM THE CITY?

A. No, I do not. My Loy admits that there are no City records which substantiate his adjustment for developer contributions and, as such, it is not appropriate to make up a scenario that significantly reduces the value of these assets to PUI. The phantom developer contributions proposed by Mr. Loy are not <u>known and measureable</u> and must be rejected by the Commission.

Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?

A. Yes. It does.